



**United States General Accounting Office  
Washington, DC 20548**

April 26, 2001

The Honorable Charles O. Rossotti  
Commissioner of Internal Revenue  
Department of the Treasury

Subject: Internal Revenue Service--Status of the Modernized Research Operations

Dear Mr. Rossotti:

In an Internal Revenue Service (IRS) memorandum from December 1999, you highlighted the importance of research in key decision-making processes and in finding ways of improving performance on IRS' strategic goals in light of limited resources.<sup>1</sup> Because we agree that using research in an effective manner is important, we monitored the status of IRS' efforts to improve its research operations. Since 1998, IRS has been undergoing a major effort to modernize its overall structure, which included the creation of four operating divisions that each focus on a particular group of taxpaying customers, such as wage earners or large businesses.<sup>2</sup> In 2000, IRS began to restructure its research organization and created, among others, research units within each of its operating divisions.<sup>3</sup>

During our review, we determined that a detailed study was not warranted at this time because IRS had made few decisions about the modernized research operations. However, from our limited work, we identified issues that present challenges for IRS management when making future decisions about research.

This letter summarizes and transmits to you information we presented in a March 15, 2001, briefing to the Deputy IRS Commissioner and other IRS officials.<sup>4</sup> In particular, this letter discusses the (1) steps IRS has taken to modernize its research operations since October 1, 2000, (2) areas of concern raised in past reports and studies of IRS research operations, and (3) status of IRS' efforts to address these concerns within the new research operations. To address these issues, we identified and summarized past studies on IRS' research organization; reviewed relevant IRS documents, such as research plans; and interviewed key officials responsible for research. We conducted

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<sup>1</sup> IRS' three strategic goals are to (1) provide top-quality service to each taxpayer in every interaction, (2) provide top-quality service to all taxpayers through fair and uniform application of the law, and (3) increase productivity through a quality work environment.

<sup>2</sup> The four operating divisions are: (1) Wage and Investment, (2) Small Business/Self-Employed, (3) Large and Mid-Size Business, and (4) Tax Exempt/Government Entities.

<sup>3</sup> In addition to the research units in the operating divisions, two other research units were created--a headquarters Office of Research and a research unit for Criminal Investigations. We refer to these units collectively as IRS' research operations.

<sup>4</sup> See enc. I for the briefing handout.

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**Abstract**

In an Internal Revenue Service (IRS) memorandum from December 1999, you highlighted the importance of research in key decision-making processes and in finding ways of improving performance on IRS' strategic goals in light of limited resources.<sup>1</sup> Because we agree that using research in an effective manner is important, we monitored the status of IRS efforts to improve its research operations. Since 1998, IRS has been undergoing a major effort to modernize its overall structure, which included the creation of four operating divisions that each focus on a particular group of taxpaying customers, such as wage earners or large businesses.<sup>2</sup> In 2000, IRS began to restructure its research organization and created, among others, research units within each of its operating divisions.<sup>3</sup> During our review, we determined that a detailed study was not warranted at this time because IRS had made few decisions about the modernized research operations. However, from our limited work, we identified issues that present challenges for IRS management when making future decisions about research. This letter summarizes and transmits to you information we presented in a March 15, 2001, briefing to the Deputy IRS Commissioner and other IRS officials.<sup>4</sup> In particular, this letter discusses the (1) steps IRS has taken to modernize its research operations since October 1, 2000, (2) areas of concern raised in past reports and studies of IRS research operations, and (3) status of IRS efforts to address these concerns within the new research operations. To address these issues, we identified and summarized past studies on IRS research organization; reviewed relevant IRS documents, such as research plans; and interviewed key officials responsible for research.

We conducted

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our work in accordance with generally accepted government auditing standards. This letter provides information on the status of IRS' efforts through February 2001.<sup>5</sup>

## Results

IRS has begun taking steps to modernize its research operations. As part of this modernization, IRS planned to create research units within each of its operating divisions to work together collaboratively. As of October 1, 2000, the assignment of research staff to the operating divisions was completed. The work for most on-going research projects continued within the new structure using interim procedures. In addition, IRS continued to place staff in key leadership positions.

Regarding the areas of concern raised in past studies of IRS research, our review of five studies conducted between 1995 and 2000 identified many concerns about IRS' research operations. (See enc. II for a list of the studies that we reviewed.) For example, four of the studies discussed the need for IRS to measure the performance of its research organization. We grouped the concerns into six general areas--research leadership, human capital, organization infrastructure, systems and data management, customer focus, and performance measures. While the specific issues from these reports may not apply to the new research structure, the overall concepts are still relevant to the new IRS research units. (See enc. I, page 8 [slides 7 and 8], for summaries of the concerns in the six general areas.)

IRS is just beginning its efforts to address these past areas of concern. IRS officials told us that, in part, they had been waiting for new research leadership to be in place before they began. As IRS addresses these concerns, the challenges still to be addressed include:

- Research Leadership--Key leadership positions within the research units were filled in January and February 2001, or remained unfilled, and a vision for research had yet to be fully developed. In addition, transitional issues, such as overcoming past perceptions that the research organization is ineffective, had not been fully addressed.
- Human Capital--The research units had numerous staff shortages compared to authorized positions. For example, in one operating division, the officials told us that about one-third of the research positions were vacant. Furthermore, the operating divisions reported inconsistencies between the mix of skills of the current staff and the skills needed to perform research; however, inventories to determine the extent of skill deficiencies had not been conducted.
- Organizational Infrastructure--The research units relied on old work processes and procedures as an interim guide for their day-to-day activities, largely because the research leaders were too new or were not available to develop new guidance. Additionally, few tools were available to assist in managing the geographically dispersed research units. For example, the Compliance Research Intranet, created

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<sup>5</sup> We excluded two research units from our review--the Tax Exempt/Government Entities Division and the Criminal Investigation unit--because these units are start-up operations that did not receive an allocation of the research staff (and projects) that existed when they started.

to record information on research projects, was less effective than it should be, according to IRS officials.

- Systems and Data Management—IRS officials told us that the data on compliance in reporting items on tax returns were outdated and that IRS did not use alternative data as fully as it could. For example, IRS officials told us about IRS data sources, such as reports of telephone services provided to taxpayers, and about external data sources, such as census data, that could be used to a greater extent as alternative sources.
- Customer Focus—While the research units have identified their internal customers, one research unit that has external customers had not completed its work to identify them. Furthermore, the research units had not determined how to involve and communicate with their customers within the new research structure.
- Performance Measures—The IRS was in the early stages of developing appropriate measures to determine the effectiveness of its research results. Some measures existed for customer satisfaction, but they were not fully developed.

During our briefing, the Deputy Commissioner and other IRS officials told us that the information we presented was accurate and timely. They suggested minor changes to improve the clarity of our information, which we made as appropriate. In addition, they provided information on additional efforts to modernize the new research units that had occurred since we completed our review. For example, the officials said that the Director of Research for the Wage and Investment Division assumed his position during March 2001.

We are sending copies of this letter to interested congressional committees. The letter is also available on GAO's home page at <http://www.gao.gov>. This letter was prepared under the direction of Tom Short. Other major contributors were Kerry Dunn, Libby Mixon, and Anthony Foster. If you have any questions about this letter, please contact Tom Short or me on (202) 512-9110.

Sincerely yours,



Michael Brostek  
Director, Tax Issues

Enclosures

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## **Abbreviations Used in GAO's Briefing**

<b>GAO</b>	General Accounting Office
<b>IRS</b>	Internal Revenue Service
<b>TIGTA</b>	Treasury Inspector General for Tax Administration
<b>SOI</b>	Statistics of Income
<b>W&amp;I</b>	Wage and Investment Operating Division
<b>SB/SE</b>	Small Business/Self-Employed Operating Division
<b>LMSB</b>	Large and Mid-Size Business Operating Division

**Briefing Handout**



**Briefing to the Deputy Commissioner  
Operations, Internal Revenue Service  
March 15, 2001**

**Status of Implementation and  
Areas of Concern in the  
Modernized IRS Research  
Organization**

1



**Modernization Effort and Importance of  
Research Prompted Study**

- Part of GAO's overall monitoring of modernization efforts
  - Congress interested in IRS' progress on modernization
  - GAO's past work on IRS' research organization raised concerns and led to inclusion of this study in GAO's strategic plan
- Commissioner Rossotti stated that research is important if IRS is to improve performance on its strategic goals

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## Objectives

- What steps has IRS taken to modernize the research organization since October 1, 2000?
- What areas of concern were raised in past reports and studies of the IRS research organization?
- What is the status of IRS' efforts to address past areas of concern within the new research organization?

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## Scope and Methodology

- Conducted literature review and held discussions with IRS officials to identify past studies of IRS research
  - TIGTA, May 2000
  - Booz-Allen and Hamilton, March 2000
  - Coopers and Lybrand Consulting, September 1998
  - GAO, June 1996
  - TIGTA, September 1995
- Reviewed studies and grouped into areas of concern

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## Scope and Methodology, continued

- Determined plans and progress, as of February 2001, in implementing modernized research organization by (1) reviewing IRS documents and (2) interviewing IRS officials in operating divisions and Office of Research
- Excluded Tax Exempt and Government Entities operating division and Criminal Investigations research units because they are start-up operations
- Our work was conducted in accordance with Generally Accepted Government Auditing Standards

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## Steps Taken to Modernize the Research Organization

- Staff transition to operating divisions complete
- The Director of Research, Analysis, and SOI and the SB/SE research director in place in February 2001
- Fiscal year 2001 research projects set in January 2001
- Work for most on-going studies continued
- Roll-over or interim procedures and processes being used

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## Past Studies Identified Concerns in Six General Areas

- Research Leadership
  - Integrate the efforts and results of the research unit into strategic decision-making efforts throughout the entity
- Human Capital
  - Ensure appropriate skills and expertise are available to perform rigorous research
- Organizational Infrastructure
  - Organize the research unit in a manner to ensure that research processes can operate as effectively and efficiently as possible to assist the overall entity

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## Past Studies Identified Concerns in Six General Areas, continued

- Systems and Data Management
  - Maintain objective data that are readily accessible for research
- Customer Focus
  - Involve and consult with research customers during all phases of a project
- Performance Measures
  - Establish and institutionalize methods to monitor project progress and determine the overall impact of research

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## Status of Efforts to Address Past Areas of Concern Within New Organization

- Officials told us of challenges facing the new research organization that mirror past areas of concern
  - Leadership: Positions, vision, transition to be addressed
  - Human Capital: Staff shortages and skill deficiencies exist
  - Organizational Infrastructure: Relies on old processes
  - Systems and Data Management: Major gaps exist
  - Customer Focus: Practices to involve customers are incomplete
  - Performance Measures: Not yet determined
- Few plans or timelines in place for new research organization in operating divisions or Office of Research to address areas of concern

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## Leadership: Positions, Vision, and Transition Still to be Addressed

- Key positions not filled
- Vision for research organization not yet fully developed
- Transition issues not fully addressed
  - Research historically viewed as somewhat ineffective
  - Research staff have and continue to face major changes

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## **Human Capital: Staff Shortages and Skill Deficiencies Exist**

- Current staff shortages; future succession planning challenges
- Inconsistent skills mix
- Incomplete skills inventory to support planning efforts

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## **Organizational Infrastructure: Primarily Relies on Old Processes**

- Incomplete work processes and procedures
- Lack of management tools for geographically-dispersed structure

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## Systems and Data Management: Major Gaps Exist

- Reporting compliance data does not exist or is outdated
- IRS is not using alternate data as fully as it could
- Additional data is needed for research
- Research intranet not fully functional

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## Customer Focus: Practices to Involve Customers Are Incomplete

- W&I, SB/SE, LMSB and Office of Research have identified internal customers
- Office of Research has yet to complete identification of external customers
- None have fully determined how to involve and communicate with their customers throughout the research process

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## Performance Measures: Not Yet Determined

- No measures set to determine effectiveness of research results
- Measures of customer satisfaction not fully developed

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## Concluding Observations

- Commissioner Rossotti underscored the importance of research to IRS' success but past concerns must be overcome to realize its potential
- While officials recognize the need to resolve past concerns, the transition to the new research organization has impeded attention to and resolution of the concerns
- It will be important for IRS to monitor progress and position itself for corrective actions
- Monitoring progress will be complicated by the lack of division-level written plans and timeframes for implementing the modernized research organization

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**Enclosure II****Studies GAO Reviewed**

Booz-Allen and Hamilton. *Research*. Discussion Document (draft), March 9, 2000.

Coopers and Lybrand Consulting. *IRS Office of Research and District Offices of Research and Analysis--Training and Organizational Assessment Project Report*. June 26, 1998.

U.S. Department of the Treasury Inspector General for Tax Administration (TIGTA). *The Internal Revenue Service Needs to Improve Control of Its Compliance Research Program*. Reference No. 2000-40-068, May 12, 2000.

U.S. Department of the Treasury Inspector General for Tax Administration (TIGTA). *Review of the National Office Research Analysis/District Office Research Analysis and Compliance Research Information System Implementation*. Reference No. 056406, September 7, 1995.

U.S. General Accounting Office. *Tax Research: IRS Has Made Progress but Major Challenges Remain*. GAO/GGD-96-109, June 5, 1996.

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